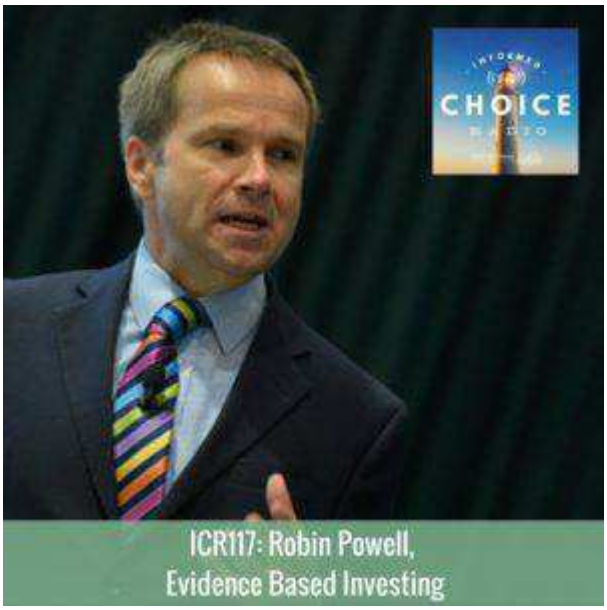
Informed Choice Radio 117:
Robin Powell, Evidence Based Investing

Hello and welcome to episode 117 of Informed Choice Radio where I speak to Robin Powell.



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Evidence based investing using index tracker funds can ignite heated debates between advisers, sometimes leaving investors wondering what to do with their portfolios.

In this episode of Informed Choice Radio, I speak to Robin Powell.

Robin was a TV reporter, producer and presenter for more than 20 years, working for Sky News, ITV and BBC 1, where he worked on The Sunday Politics. He reported from locations including Baghdad, Soweto and Guantanamo Bay, and made award-winning documentaries on the Holocaust and on Britain's Romany Gypsy community.

He is the founder of Ember Television, a television and online video production company based in Birmingham. Notable clients include The Royal Shakespeare Company, The Church of England, Birmingham City Council, University of Warwick and Incisive Media.

For three years, Robin was a consultant to Sensible Investing TV, for whom he produced and presented the highly acclaimed online documentary How to Win the Loser's Game. He also works as a brand journalist and content marketing consultant for advisers in Europe, North America and Australasia.

Robin is a member of the Chartered Institute of Journalists and was a Visiting Media Fellow at Duke University in North Carolina. Married with two children, Robin lives in rural North Warwickshire and works in Birmingham.

In this episode of Informed Choice Radio, I speak to Robin about his move to producing tailored content for financial services, what sparked his passion for evidence based investing, whether index funds have reached a tipping point and will become more popular than actively managed funds, and much more.

Welcome to Evidence Based Investing with Robin Powell, in episode 117 of Informed Choice Radio.

Martin: Robin, welcome to Informed Choice Radio. Thank you so much for joining us on the show. Could you start by telling our listeners a little bit about you and about your background?

Robin: Yes. I'm a journalist. I started in local newspapers, worked in radio for a while, and then joined ITV Central in the Oxfordshire area initially and then moved up to Birmingham. I've since worked for Sky News and for the Politics show on BBC 1. Yeah, so I've had a pretty varied journalistic career.

I suppose I would now describe myself as a brand journalist. In a sense I work for brands, largely financial brands, to help them get their message across, and particularly with financial advisors helping them to attract and retain clients and also to educate their clients.

Martin: We'll come on to talk in just a second about the work you do with financial brands and that element of it, but I was looking at your Wikipedia page before we started chatting, and it's fascinating background there. You've reported from Baghdad and from Soweto, from Guantanamo Bay. If you were to go back through your broadcasting career and maybe pick out a few of your best moments, what would they be?

Robin: One of the most interesting assignments was in Baghdad in the days of Saddam Hussein, before the second Gulf War when the west was imposing sanctions on Iraq. Very few journalists were actually telling the story on the ground there at that time, and it was a real privilege to do so. I was one of the first British journalists as well to go to Guantanamo Bay and to highlight the issues there. The pretty tough times that the British detainees in particular were going through there. Many of them there without having had any proper trial. Were really waiting there for years without having any chance to answer the allegations that were being made against them. That was a really exciting story to report on.

I'll be quite honest with you Martin, I actually think that although this whole transparency and asset management thing might seem quite dry in comparison to Iraq under Saddam or Guantanamo Bay. I actually find this story in a sense an even bigger one.

We here have an industry that is thoroughly dominant in terms of its political influence, its financial clout, and its advertising budget and so on. Which to a large extent is enriching itself

at the expense of ordinary consumers. All over the world we have tens of thousands of people who are retiring every week without enough funds to last them for the rest of their lives. For me, that is a massive story on a global scale, and as a journalist I think this is so important a story, so big a story, that I'm pretty well devoting a hundred percent of my time to telling that story.

Martin: You've moved from the trouble zones of Baghdad and Gitmo to the dodgy world of financial services, and we'll come on pick that one up in a second. You're founder of Ember Television which produces videos with tailor content for the financial services sector in the main. What made you decide to make that transition then from ... Obviously you've just explained there, there was a story there, and a story you wanted to tell. What were the drivers behind that transition from mainstream political and geopolitical broadcasting to more tailored content for financial services?

Robin: It actually happened by accident. You get to a stage in your early forties where you're starting to develop a face for radio rather than television or audio podcasting or just simple writing if you like. I saw that my future was outside of mainstream television, and quite by chance we were approached by a company here in Birmingham, Barnett Ravenscroft Wealth Management, who took this evidence-based approach to investing. They said, "Look, we work mainly with high net worth clients but we feel there is a bigger story here for ordinary investors, a story that we need to get out there." They said, "We're thinking of writing a book, but another idea that we had is some kind of online documentary."

Being an online documentary maker I persuaded them to go down the second route. We made a very successful program about seventy-five minutes long called Passive Investing The Evidence, for which we interviewed a number of really key players, Jack Bogle at Vanguard, David Booth at Dimensional, the Nobel Prize winning economist William Sharpe in California. Some really big names, if you like.

I must say I'd been quite skeptical until then about passive investing. I suppose largely from what my own advisors had told me in the past. Also from what I read in the papers. You probably know Martin that the papers up until very recently have not have had very much to say about index funds, and if they've said anything about them it's more or less that they're

cheap and not as good as high fee active funds. Speaking to the likes of Bogle and Sharpe and Charlie Ellis, these sorts of people. I just started to realize what's going on here? The way that ninety percent of people invest is completely bonkers. What are we doing? It was really at that point that I decided that this is my challenge in my career now, that I really want to work at educating investors about the best way to invest.

Martin: Anyone who follows you on Twitter will be conscious you're very passionate when it comes to index investing. Was it solely that documentary which convinced you, so speaking to those various experts and hearing the arguments about evidence-based investing. Was that almost the awakening in your life when it came to that approach to index investing?

Robin: I suppose it was. Another expert we interviewed for that program, Rick Ferri, an advisor and author in the United States and a very popular blogger, said that in his experience people have what he called a light bulb moment with evidence-based investing. You know, they read books, they read articles, they listen to the arguments, and eventually they say, "I get it." Yeah, somewhere through that ... Can't remember the exact Damascene moment where it happened, but sometime during the making of that documentary I decided, "Yeah, this is true. The evidence is completely compelling, absolutely compelling."

Martin: If we could just take things back to basics for a moment for our listeners that don't know what we're talking here when we're talking about index tracker funds and evidence-based investing, how would you sum that up in a nutshell? What are they, how do they work?

Robin: An index fund contains simply all the stocks ... Actually, I say stocks, it could be bonds as well because there are fixed income index funds too. By investing in one you are effectively saying, "I don't know which stocks are going to be the winners, which are going to be the losers, but I know looking at historical performance that generally that markets, equity markets in particular, have been generous to those who are disciplined and patient, and I'm going to invest in the whole market." Effectively, index funds just track the index, all the stocks or assets in a particular index.

Martin: You mentioned a moment ago that around ninety percent of retail investors are still going into high fee active funds. My maths isn't great but about ten percent that means going to

index trackers. I think the latest stats I saw from the IA were about eleven percent, so it is rising slightly, but we still lag behind the US market I believe, when it comes to popularity of index funds for investors. Do you think they are becoming a more popular choice and at some point do you think they'll become an even more popular choice than high fee active manage funds?

Robin: Undoubtedly, they are becoming much more popular. You mentioned the US there. I was actually reading only this morning in the Financial Times, that if things continue at their current rate, the flows out of active funds and into passive funds in the US equity markets, then passive is going to account for more than fifty percent of all assets under management in the US within three to five years. That is the prediction of Morning Star.

We are a lot further behind here in the UK, but there is no doubt that things are moving in that direction. Only a couple of days ago we heard that Hargreaves Lansdown, Britain's biggest broker, which for many years has been promoting high fee funds over low cost passive style alternatives, has now said, "Right, yeah, we're going to include index funds in our list of so called favorite or recommended funds." Things are definitely moving in the right direction, it's happening in Australasia, it's happening in Africa as well, I spoke at a conference there just a few weeks ago, and very exciting to see really from a very small base, evidence-based investing starting to take off.

Martin: Is it fair to say that all index tracker funds are the same? Or are some very different? There's almost a hybrid I think, out there, with some which are trying to make more active investment decisions. I've heard the term 'smart beta' used recently. Do you think that can work, or is that just as bad as a high fee active fund in your opinion?

Robin: Broadly speaking there are two different types of passive fund. One is what I suppose would call 'market cap weighted index fund', and that effectively reflects the market weighting of each stock in a particular index. For example, if you have a FTSE 250 funds, the largest stocks will account for the largest holdings in your portfolio. That's called, as I say, 'market cap weighting'. I suppose that's indexing in its purest forms. Without getting technical there are other types, there's for example, equal weighting index funds, which actually do have a lot going for them, and I don't think we have enough equal weighted index funds.

Getting aside from those technicalities the second broad type of passive fund, (now a lot of people would say they're not passive at all they're active, I would actually say they're actually more passive than active) are ... You mentioned the term 'smart beta', these are funds which give the investor exposure to risk factors which academics over many decades have identified as producing higher long term returns.

There are different types of risk factors. I suppose the largest ones are small companies, in other words, the smaller companies although often give you more volatility, also over the long term generally, not always, not guaranteed, but generally produce higher returns for patient investors. The other major factor is value, so in other words, value stocks are likely to deliver higher long term returns than so called growth stocks. There are other factors as well, momentum is one that is being talked about quite a lot at the moment. Effectively, with smart beta, to be honest I don't like calling it smart beta, beta for me is just beta, it's another type of risk. All investing involves a degree of risk, generally speaking the more risk you take the higher your expected returns. Again, that's not guaranteed, but the higher your expected returns will be. Should people be going into smart beta funds? That's entirely up to them. If they're willing to take on that extra risk of tilting their portfolio, to use the expression the industry like to use, tilting their portfolio to small caps or to value stocks, yes, the evidence shows that in the long term that should deliver higher returns, but you can expect greater risk or at least great volatility in the meantime.

Martin: Again, without wanting to get too technical on the subject, replication is an issue for some index funds at least. We see some index funds which actually generate quite a different return to the underlying index they're trying to track. How can investors identify index trackers which best replicate their chosen index and best suit what they're trying to achieve?

Robin: This is an issue that people who promote active funds like to make a big thing of. Yes, it is almost impossible to replicate an index one hundred percent, so therefore you're going to get some degree of tracking difference. Tracking difference typically is about ten basis points, and by basis points we mean one basis point is 0.01 percent, so we're talking about something really very small. There are some funds which have slightly better or lower tracking error than others, and clearly it pays to look out for the tracking difference, because effectively that is a

cost of using an index fund, as well as the ongoing charge you've also got to think of the tracking difference in terms of cost. When you add up the tracking difference to the annual charge, the cost of using an index fund is hugely lower, and I do mean hugely lower, than for using an active fund.

Martin: Continuing to play a bit of devil's advocate here, another thing that we often hear from those that advocate the high fee active manage funds is that if everyone in the world used an index fund markets simply wouldn't function, or at least it would amplify into stock market volatility to a great extent. Is that a fair comment?

Robin: We're hearing quite a lot about this at the moment. There was a quite ridiculous paper that came round, was doing the rounds last week for example, which likened indexing to Marxism, saying effectively that it undermined capitalism, which to be honest says much more about the desperation of the vested interests who want to keep the status quo more than anything else.

When you hear these horror stories about what's going to happen if everyone starts indexing, what you've got to remember is that indexing is still a relatively small part of the market. Okay, in the United States it is becoming increasingly popular. In the UK we are nowhere near those levels yet. If you think about it as well, there has been over the last two or three decades, people talk about an indexing bubble, there's been a closet indexing bubble.

In other words, active fund managers have been charging high active fund fees for funds which pretty well sale close to the index, pretty well guaranteeing that manager a reasonable performance that's not going to be too bad compared with the market index. You don't see the active fund industry jumping up and down worrying about the closet indexing bubble that we've had for the last twenty years or so.

The other thing to remember is that if we ever came to that stage where almost everyone indexed, and quite honestly I cannot see it happening because of human nature, we all like to think we can beat the market, there will always be people who will try to do it, there will always be people who are happy to take the money off people who want to give it a try, in other words there will always be fund managers out there who want to earn a good living out of it.

If we ever got to the point where almost everyone indexed, then clearly we would start to see inefficiency in the market, and it would start to pay to use active funds. Heck, even I would actually use an active fund if we ever came to that point, but frankly it is not going to happen.

You should never say never, but I am pretty well a hundred percent certain that that will never happen. It certainly won't happen in our lifetimes. I remember speaking to William Bernstein for our first documentary. William Bernstein, a very respected, hugely intelligent investment expert based in the US. He was saying his guess is that eventually it will level out at around fifty percent passive, fifty percent active. He's such a clever guy I wouldn't like to argue with him.

Martin: Can some funds beat the market, is it possible? I've seen academic research in the past that suggests that funds which have a very high active share, so the polar opposite of those closet index trackers that you mentioned, can potentially do it. Is it fair to say that there's a place for both index funds and actively managed funds if you choose the right actively managed funds?

Robin: Of course active funds can beat the market. Of course some funds will beat the market; just simply by the law of averages some funds will beat the market. Martin, you could win the lottery on Saturday night. Aston Villa could win the Champions League in three years' time. It might happen, but the chances are, sadly in the latter case from my own point of view, it's not going to happen. Active management is the triumph of hope and marketing over the evidence, and the evidence shows that no more active funds beat the market than you would expect by random chance. It's honestly as bad as that. Around one percent of funds over the long term beat the index. Can you spot them? All the evidence again suggests it's almost impossible to spot future winners in advance.

Martin: Robin, thank you so much for being on the show today. That was a really interesting discussion, I'm sure our listeners will get a great deal of value from that. Before you go, are there any social media links or websites you'd like to share with our audience?

Robin: Thank you very much for having me Martin. I'd love people to comment on my blog The Evidence-Based Investor, EvidenceInvestor.com. You can follow me on Twitter

@RobinJPowell. Yeah, join in the discussion; I'd love to debate this issue with you.

Martin: Fantastic. I'd highly recommend people follow you on Twitter @RobinJPowell. I think some of the links and the articles you post on there are really worth reading, and I often enjoy seeing you getting into good debates and discussions with other people as well. We'll post those links and I'll show notes of this episode so people can find it nice and easily. Robin, thank you for your time today, it's been fantastic.

Robin: It's been a pleasure, thank you.

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